

JULY 24, 2018

Equity	% Chg				
	23-Jul	1 Day	1 Mth	3 Mths	
Indian Indices					
SENSEX Index	36,719	0.6	2.9	6.1	
NIFTY Index	11,085	0.7	2.4	4.4	
NSEBANK Index	27,008	0.5	0.9	7.9	
NIFTY 500 Index	9,364	0.8	0.7	(0.3)	
CNXMcap Index	18,255	1.1	(1.8)	(8.7)	
BSESMCAP Index	15,867	0.9	(4.1)	(13.1)	
World Indices					
Dow Jones	25,044	(0.1)	1.9	4.2	
Nasdaq	7,842	0.3	1.9	11.9	
FTSE	7,656	(0.3)	(0.3)	3.1	
NIKKEI	22,397	(1.3)	0.0	1.1	
Hangseng	22,397	(1.3)	0.0	1.1	
Shanghai	28,256	0.1	(2.5)	(6.6)	
Value traded (Rs cr)		23-Jul	% Chg Day		
Cash BSE		2,582	(6.7)		
Cash NSE		31,562	8.2		
Derivatives		685,819	30.7		
Net inflows (Rs cr)		20-Jul	MTD	YTD	
FII		335	(2,262)	(7,101)	
Mutual Fund		(199)	5,512	74,115	
Nifty Gainers & Losers		Price	Chg	Vol	
23-Jul		(Rs)	(%)	(mn)	
Gainers					
UPL Ltd		632	15.0	23.8	
Vedanta Ltd		212	4.6	8.9	
Bharti Airtel		359	3.9	3.7	
Losers					
Hero MotoCorp		3,165	(6.3)	1.9	
Bajaj Auto		2,684	(5.5)	3.0	
Wipro		276	(2.3)	8.8	
Advances / Declines (BSE)					
23-Jul	A	B	T	Total	% total
Advances	280	646	67	993	100
Declines	105	402	62	569	57
Unchanged	3	25	21	49	5
Commodity		% Chg			
	23-Jul	1 Day	1 Mth	3 Mths	
Crude (US\$/BBL)	72.8	(0.4)	(3.6)	(1.4)	
Gold (US\$/OZ)	1,224	(0.6)	(3.6)	(8.1)	
Silver (US\$/OZ)	15.4	(0.9)	(6.4)	(7.9)	
Debt / forex market		23-Jul	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %		7.8	7.8	7.8	7.7
Re/US\$		68.9	68.9	68.1	66.5



Source: Bloomberg

News Highlights

- ▶ The Lok Sabha In a bid to reduce the number of cheque dishonor cases pending in courts, has passed the Negotiable Instruments (Amendment) Bill, 2017 as part of its monsoon session activity. (Mint)
- ▶ Twenty-four banks led by the SBI yesterday signed the inter-creditor agreement that aims to fast-track the resolution of bad loans. The banks include Seventeen public sector banks, five private sector banks and two other financial institutions. (Mint)
- ▶ The fourth sitting of the monsoon session of Parliament saw the government giving a push to its legislative agenda with six bills introduced and two passed in the Lok Sabha while three bills were taken up for passage in the Rajya Sabha. (ET)
- ▶ The finance ministry is planning to transfer government shares of 10 PSUs, including **MMTC, ITDC, MRPL, Hindustan Copper**, to a fund to meet Securities and Exchange Board of India's (Sebi) minimum public shareholding norms. (Mint)
- ▶ Syngene International, the contract research arm of **Biocon** has expanded the scope of its research and development (R&D) efforts with Baxter Health Corporation.(BL)
- ▶ **Essel Propack** has commenced the First phase of commercial production at its new unit in Assam.In the first phase, the facility is equipped to produce 200 mn tubes per annum and will ramp up to 750 mn tubes over a span of 18 months. (BL)
- ▶ The merger between **Idea** and Vodafone has moved a step closer with the companies settling all their dues with the Department of Telecom (DoT). This includes Rs 39 bn in cash by vodafone and Rs 33 bn in bank guarantees by idea , totalling Rs 72 bn. (Mint)
- ▶ **Indian Energy Exchange Ltd** has informed BSE that a meeting of the Board of Directors of the Company is scheduled to be held on August 09, 2018, to consider sub division of face value of equity shares of the Company. (BL)
- ▶ **Infosys Ltd** has, for the first time, linked incentives of six of its top employees to how much revenue the company generates from digital technologies. (Mint)
- ▶ Standard Chartered Bank has opened a credit line of Rs 35 bn for Vedanta to help finance the purchase of **Electrosteel**, the second biggest bad loans resolution under the Insolvency and Bankruptcy Code (IBC). (ET)
- ▶ Fitch yesterday revised its ratings outlook on **UPL Corp** to negative from stable, citing an increase in the company's leverage. But Fitch has affirmed its long-term foreign-currency issuer default rating at BBB-. (ET)
- ▶ **IZMO limited** has won a big multi-crore order from a leading OEM in Mexico for its innovative Car Visualiser Product, a unique solution which provides extremely high quality multi-media content for the desktop and more importantly, the mobile market. (BS)

What's Inside

- ▶ **Result Update:** Bajaj Auto Ltd, Hindustan Zinc Ltd

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, IE = Indian Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange, MC = Moneycontrol

Result Update

BAJAJ AUTO LTD (BAL)

Stock Details

Market cap (Rs mn)	:	776704
52-wk Hi/Lo (Rs)	:	3473 / 2655
Face Value (Rs)	:	10
3M Avg. daily vol	:	614,607
Shares o/s (m)	:	289

Source: Bloomberg

Financial Summary

Y/E Mar (Rs mn)	FY18	FY19E	FY20E
Revenues	251,649	291,677	324,574
Growth (%)	15.6	15.9	11.3
EBITDA	47,834	50,419	56,491
EBITDA margin (%)	19.0	17.3	17.4
Net profit	40,681	42,616	47,795
EPS (Rs)	140.6	147.3	165.2
Growth (%)	6.3	4.8	12.2
Book value (Rs/share)	660	735	822
Dividend per share (Rs)	60	65	70
ROE (%)	22.7	21.1	21.2
ROCE (%)	31.4	29.9	30.2
P/E (x)	19.0	18.3	16.3
EV/EBITDA (x)	14.9	13.8	11.9
P/BV (x)	4.1	3.7	3.3

Source: Company

Shareholding Pattern (%)

(%)	Jun-18	Mar-18	Dec-17
Promoters	49.3	49.3	49.3
FII	16.7	17.2	17.2
DII	7.9	8.5	8.8
Others	26.0	25.0	24.7

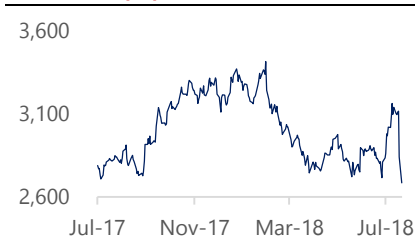
Source: Company

Price Performance (%)

(%)	1M	3M	6M
Bajaj Auto	(5.2)	(5.9)	(18.6)
Nifty	2.4	4.7	0.0

Source: Bloomberg

Price chart (Rs)



Source: Bloomberg

PRICE Rs.2684

TARGET Rs.2808

REDUCE

BAL reported below expected 1QFY19 results. Lower domestic average selling price impacted revenues, EBITDA and PAT for the quarter. Company reported robust volume growth and market share gain in 1QFY19. Company's decision to go for aggressive pricing to gain market share will impact its financial performance going ahead.

Key Highlights

Revenues for the quarter grew by 36% YoY, supported by 38% increase in sales volume. Average selling price in the quarter declined by 1.3% YoY and was lower than expected. EBITDA in the quarter grew by 36.6% YoY and EBITDA margin improved by 10bps, but was well below estimates. PAT for the quarter at Rs11.2bn grew by 21% YoY but came in 8% below estimates.

Valuation and Outlook

BAL has stated that gaining market share will be the key focus in the domestic motorcycle segment. Pricing action has translated into significant growth for the company (in past few months) in the entry level segment and the same will likely continue in view of management's decision to stick to this strategy. In view of management's strategy of gaining market share at the expense of margin, we revise our estimates lower. We downgrade the stock to REDCUE (from BUY earlier) with revised price target of Rs2,808 (earlier Rs3,303).

Quarterly performance

(Rs mn)	1QFY19	1QFY18	YoY (%)	4QFY18	QoQ (%)
Revenues	74,193	54,424	36.3	67,733	9.5
Total expenditure	61,379	45,040	36.3	54,581	12.5
RM consumed	52,993	38,093	39.1	46,969	12.8
Employee cost	3,140	2,725	15.2	2,670	17.6
Other expenses	5,246	4,222	24.2	4,942	6.2
EBITDA	12,814	9,384	36.6	13,152	(2.6)
EBITDA margin (%)	17.3	17.2	-	19.4	-
Depreciation	700	753	(7.0)	879	(20.4)
Interest cost	3	2	29.2	3	3
Other Income	4,044	4,573	(11.6)	3,667	10.3
Exceptional Items		(320)			
PBT	16,156	12,881	25.4	15,937	1.4
PBT margins (%)	21.8	23.7		23.5	
Tax	5,003	3,642	37.4	5,138	(2.6)
Tax rate (%)	31.0	28.3	-	32.2	-
Reported PAT	11,152	9,239	20.7	10,799	3.3
PAT margins (%)	15.0	17.0	-	15.9	-
EPS (Rs)	38.5	31.9	20.7	37.3	3.3
Total Volumes	1,226,641	888,434	38.1	1,045,378	17.3
ASP (Rs)	60,485	61,258	(1.3)	64,793	(6.6)
RM cost per vehicle (Rs)	43,201	42,876	0.8	44,931	(3.8)

Source: Company

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Result Highlights

BAL reported revenue of Rs74.2bn, 36% growth over 1QFY18. Growth in revenue was driven by 38% YoY higher volumes – 33% / 74% YoY increase in two / three wheeler volumes respectively. In the entry level domestic motorcycle segment, YoY volume growth stood at 74% (led by 76% growth in CT100 volumes), translating into market share rising to 33.7% in 1QFY19 (increase of 850bps). Pulsar segment too witnessed strong growth in volumes in the quarter. Domestic 3W volumes increased by 80% YoY. Average selling price in the domestic market declined by 12.8% QoQ (due to weak product mix) and came in below expectation. Export volumes in the quarter grew by 31% YoY, led by recovery in traditional markets (Nigeria, Egypt) and growing presence in new markets. 1QFY19 export revenue came in at \$444mn as against \$347mn in 1QFY18 and \$343mn in 4QFY18. USD realization was Rs67.4 in 1QFY19 as against Rs66.8 in 1QFY18 and Rs67.2 in 4QFY18. Spare revenue in the quarter was Rs6.5bn (includes Rs1.9bn from exports), 8% higher YoY.

EBITDA in 1QFY19 came in at Rs12.8bn, 37% growth YoY, but was lower than our expectation. Lower than estimated EBITDA was on account of 4% miss on revenues and sharp increase in raw material cost. Gross margin declined from 30% in 1QFY18 and 30.7% in 4QFY18 to 28.6% in 1QFY19. Higher commodity price, weak product mix and price cut in key product impacted gross margin in the quarter. On a per vehicle basis, employee cost and other expenses were by down 17% and 10% respectively on account of operating leverage from higher volumes.

Other income declined YoY on account of lower investment income in the quarter. Tax rate in the quarter was slightly higher YoY. BAL reported PAT of Rs11.2bn in 1QFY19, 21% growth over 1QFY18. Adjusted PAT grew by 17% YoY. Reported PAT was 8% lower than our estimates.

Conference Call Highlights

- Management has set a sales volume target of 4.8mn units in FY19, as against 4mn units sold in FY18.
- In the domestic motorcycle segment, the management highlighted that the company will focus on increasing market share in the entry level domestic motorcycle segment (from current ~34% to 45-50%) through aggressive pricing strategy. Company is optimistic on strong growth of CT branded motorcycle. BAL sells motorcycle under the CT brand at a loss. Management has undertaken product/pricing action for the Pulsar brand to expand the segment. Company is targeting 2.4mn motorcycle sales volume in the domestic segment in FY19.
- Management is expecting to sell ~375,000 – 400,000 three wheelers in the domestic market in FY19. Strong volume growth in 1QFY19 and robust performance in the diesel and cargo segment is expected to support growth.
- In exports, management is looking at sales volume of 2mn units in FY19. Company expects that at the current level of INR, USD realization will increase by Rs0.5. In FY19, management is expecting USD/INR realization of Rs68 in exports.
- On the back of aggressive pricing strategy adopted in the entry level motorcycle segment, the management expects EBIDTA margin to stay impacted.
- Inventory level is round 5 weeks. Company is facing production constraint for CT model. In FY19, cpaex is expected to be ~Rs3bn. Going ahead, as new capacities will be required, capex will increase to Rs5bn per annum.

- While majority of raw material cost increased is passed through, management expects some more impact in 2QFY18 on account of higher price commanded by vendors. BAL took price hikes in April/May 2018. In July 2018, BAL took another price hike of Rs300-450 per motorcycle in domestic market (except entry level segment) and Rs1,000-1,500 in the three wheeler segment.

Outlook and Valuations

BAL has stated that gaining market share will be the key focus in the domestic motorcycle segment. Company expects that pricing action taken in the entry level segment (for Brand CT) will lead to expanding the segment and help the company in gaining market share. Under the Pulsar brand too, the company has introduced product at lower price point.

Company highlighted that its margins in the other segments (forming ~86% of the revenues) remains unchanged. Domestic entry level segment accounts for ~14% of the revenues and the company is incurring loss in this segment (CT brand).

Pricing action has translated into significant volume growth for the company (in past few months) in the entry level segment and the same will likely continue in view of management's decision to stick to this strategy. This move will impact BAL's EBITDA margin as CT is a loss making product.

In view of management's strategy of gaining market share at the expense of margin, we revise our estimates lower. While we increase our volume assumption, we cut our margin and net profit estimates.

We downgrade the stock to REDCUE (from BUY earlier) with revised price target of R2,808 (earlier Rs3,303). We lower our target PE multiple from 18x to 17x.

Change in estimates

(Rs mn)	FY19			FY20		
	Old	New	% chg	Old	New	% chg
Revenues	283,928	291,677	2.7	319,287	324,574	1.7
EBITDA margin (%)	19.2	17.3	-	19.4	17.4	-
Adjusted PAT	46,631	42,616	(8.6)	53,095	47,795	(10.0)

Source: Kotak Securities – Private Client Research

Key Risk

Aggressive pricing strategy in other segments can further impact EBITDA margin and net profits

Company Background

Bajaj Auto is the flagship company of Bajaj Group. In the domestic two wheeler segment, the company is the fourth largest player with 10% market share (~16% market share in the domestic motorcycle segment). Bajaj Auto is India's largest exporter of both motorcycles and three-wheelers and it enjoys significant market shares. In terms of segment -mix, 84% volume comes from two wheeler segment and 16% from three wheeler segment. Bajaj Auto sells ~60% of the volumes in the domestic market and balance 40% is exported. Company has plant at Waluj (annual capacity – 3.6mn units), Chakan (annual capacity – 1.2mn units) and Pantnagar (annual capacity – 1.8mn units) Bajaj Auto holds approximately 48% stake in KTM AG of Austria

Financials: Standalone

Profit and Loss Statement (Rs mn)

(Year-end March)	FY17	FY18	FY19E	FY20E
Revenues	217,667	251,649	291,677	324,574
% change YoY	(3.6)	15.6	15.9	11.3
EBITDA	44,224	47,834	50,419	56,491
% change YoY	(7.5)	8.2	5.4	12.0
Depreciation	3,073	3,148	3,266	3,504
EBIT	41,151	44,686	47,153	52,987
% change YoY	(8.0)	8.6	5.5	12.4
Net interest	14	13	15	15
Other Income	12,220	13,473	14,625	16,295
Exceptional income/(loss)	0	(320)	0	0
Profit before tax	53,356	57,826	61,763	69,267
% change YoY	(3.8)	8.4	6.8	12.2
Tax	15,081	17,145	19,146	21,473
as % of PBT	28.3	29.6	31.0	31.0
Profit after tax	38,276	40,681	42,616	47,795
Adjusted PAT	38,276	41,001	42,616	47,795
% change YoY	(2.6)	7.1	3.9	12.2
Shares outstanding (m)	289	289	289	289
Adjusted EPS (Rs)	132.3	141.7	147.3	165.2
DPS (Rs)	55.0	60.0	65.0	70.0

Source: Company, Kotak Securities – Private Client Research

Cash flow Statement

(Year-end March)	FY17	FY18	FY19E	FY20E
EBIT	41,151	44,686	47,153	52,987
Depreciation	3,073	3,148	3,266	3,504
Change in working capital	(360)	4,558	(1,543)	(1,247)
Chg in other net current asset	(338)	6,958	(260)	(142)
Operating cash flow	43,526	59,350	48,615	55,102
Interest	(14)	(13)	(15)	(15)
Tax	(13,973)	(17,047)	(19,146)	(21,473)
Other Income	12,220	13,473	14,625	16,295
EO income	-	(320)	-	-
Others	1,142	(828)	-	-
CF from operations	42,900	54,615	44,079	49,910
Capex	(2,129)	(2,056)	(3,000)	(4,000)
(Inc)/dec in investments	(44,709)	(28,569)	(22,346)	(25,000)
CF from investments	(46,838)	(30,625)	(25,346)	(29,000)
Proceeds from issue of equities	-	-	-	-
Inc/(dec) in debt	20	9	-	-
Proceeds from share premium	-	-	-	-
Dividends	(1,741)	(19,155)	(20,930)	(22,759)
CF financing	(1,721)	(19,146)	(20,930)	(22,759)
Opening cash	8,595	2,937	7,780	5,582
Closing cash	2,937	7,780	5,582	3,734

Source: Company, Kotak Securities – Private Client Research

Balance sheet (Rs mn)

(Year-end March)	FY17	FY18	FY19E	FY20E
Cash and cash equivalents	63,438	65,434	85,582	108,734
Accounts receivable	9,533	14,919	15,982	17,785
Inventories	7,284	7,426	9,025	10,476
Loans and Adv & Others	20,641	12,839	13,812	14,707
Current assets	100,895	100,618	124,402	151,702
LT investments	86,814	118,229	118,229	118,229
Net fixed assets	20,440	19,348	19,082	19,578
Total assets	208,149	238,195	261,714	289,510
Payables	22,357	32,443	33,563	35,570
Other liabilities	9,125	7,893	8,374	8,886
Current Liabilities	31,482	40,337	41,936	44,456
Provisions	1,991	2,378	2,610	2,851
Deferred Tax Liability	3,136	3,234	3,234	3,234
Debt	1,199	1,208	1,208	1,208
Equity	2,894	2,894	2,894	2,894
Reserves	167,448	188,145	209,831	234,867
Total liabilities	208,149	238,195	261,714	289,510

Source: Company, Kotak Securities – Private Client Research;

Ratio Analysis

(Year-end March)	FY17	FY18	FY19E	FY20E
Margins				
EBITDA margin (%)	20.3	19.0	17.3	17.4
EBIT margin (%)	18.9	17.8	16.2	16.3
Adj. net profit margin (%)	17.6	16.3	14.6	14.7
Working capital days				
Inventory (days)	12	11	11	12
Receivable (days)	16	22	20	20
Payable (days)	37	47	42	40
Ratios				
Debt/equity ratio (x)	0.0	0.0	0.0	0.0
ROE (%)	25.3	22.7	21.1	21.2
ROCE (%)	34.4	31.4	29.9	30.2
Valuations				
EV/ Sales	3.3	2.8	2.4	2.1
EV/EBITDA	16.2	14.9	13.8	11.9
Price to earnings (P/E)	20.3	19.0	18.3	16.3
Price to book value (P/B)	4.6	4.1	3.7	3.3

Source: Company, Kotak Securities – Private Client Research

Result Update

Stock Details

Market cap (Rs mn)	:	1131118
52-wk Hi/Lo (Rs)	:	340 / 261
Face Value (Rs)	:	2
3M Avg. daily volume	:	1,987,933
Shares o/s (m)	:	4225

Source: Bloomberg

Financial Summary

Y/E Mar (Rs mn)	FY18	FY19E	FY20E
Revenue	225,210	259,484	272,056
Growth (%)	19.8	15.2	4.8
EBITDA	122,720	140,247	148,163
EBITDA margin (%)	54.5	54.0	54.5
PAT	92,760	95,988	101,770
EPS	22.0	22.7	24.1
EPS Growth (%)	11.5	3.5	6.0
BV (Rs/share)	85	96	108
Dividend/share (Rs)	8.0	10.0	10.0
ROE (%)	26.4	24.2	22.6
ROCE (%)	26.4	24.1	22.6
P/E (x)	12.2	11.8	11.1
EV/EBITDA (x)	7.4	6.2	5.6
P/BV (x)	3.2	2.8	2.5

Source: Company

Shareholding Pattern (%)

(%)	Jun-18	Mar-18	Dec-17
Promoters	64.9	64.9	64.9
FII	2.0	2.3	2.2
DII	2.0	1.5	1.6
Others	1.5	31.3	31.3

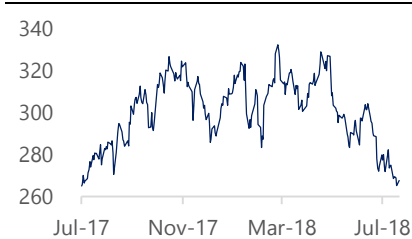
Source: Company

Price Performance (%)

(%)	1M	3M	6M
Hindustan Zinc	(7.4)	(17.2)	(9.8)
Nifty	2.4	4.7	0.0

Source: Bloomberg

Price chart (Rs)



Source: Bloomberg

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HINDUSTAN ZINC LTD

PRICE Rs.268

TARGET Rs.300

BUY

HZ's Q1FY19 performance was weak due to miss at operating level (lower volume and increase in the cost of production) and lower other income. The expansion to 1.2MT mined metal capacity is in its final stages and management expects to achieve a production run-rate by 4QFY19, this will led by the start of production shafts at RA/SK underground mines from 3QFY19.

Key Highlights

- Zinc production declined 11%/17% YoY/QoQ due to lower availability of zinc mined metal. Lead production declined 16% QoQ due to maintenance shutdown, resulting in 19% QoQ decline in silver production.
- Cost of production in 1QFY19 increased to US\$1,043/tonne due to lower volume, higher power & fuel costs, and wage settlement.
- PAT was lower than estimate due to 41.8%/38.5% YoY/QoQ decline in other income to Rs2.99 bn, due to MTM loss on debt instruments.
- Mined metal and refined zinc-lead production in FY19 is expected to increase progressively with the ramp-up of underground mines. Silver production is expected to be in the range of 650-700MT.

Valuation & outlook

Zinc prices corrected in the recent past due to trade war and increase in zinc inventory (surplus in 1QFY19). However, as per ILZSG, zinc market is expected to remain in deficit in 2018 and we foresee the HZ to benefit from the favorable zinc environment. Besides this, given its presences in the lower end of the cost curve globally (backed by high grade captive mines), diversified revenue stream with an increasing contribution from silver and strong balance sheet augurs well for the company. Due to lower than expected 1QFY19, we have revised our estimates to Rs22.7 (earlier Rs24.4) and Rs24.1 (earlier Rs25.8) for FY19E and FY20E, respectively. The stock has corrected since our last recommendation (Reduce at CMP Rs.308) and now is trading at 6.2x/5.6x FY19E/FY20E EV/EBITDA, which in our view is attractive. Hence, we upgrade the stock to BUY, with a revised target price of Rs300 (earlier Rs318).

Quarterly performance table

Y/E March (Rsmn)	Q1FY19	Q1FY18	YoY (%)	Q4FY18	QoQ (%)
Net sales	53,100	50,130	5.9	62,770	(15.4)
Consumption of RM	11120	10610		12890	
Other Expenditure	12,530	13,940		11,860	
Total Cost	25,970	26,290		26,570	
EBITDA	27,130	23,840	13.8	36,200	(25.1)
EBITDA Margin (%)	51.1	47.6		57.7	
Depreciation	3,870	3,260		4,590	
Interest	150	1370		450	
EBT	23,110	19,210		31,160	
Other income	2990	5140		4860	
PBT	26,100	24,350	7.2	36,020	(27.5)
Exceptional Items	0	0		(510)	
Provision for tax	6,920	5,460		10,460	
Effective Tax Rate %	26.5	22.4		29.0	
PAT (reported)	19,180	18,890	1.5	25,050	(23.4)
NPM (%)	36.1	37.7		39.9	

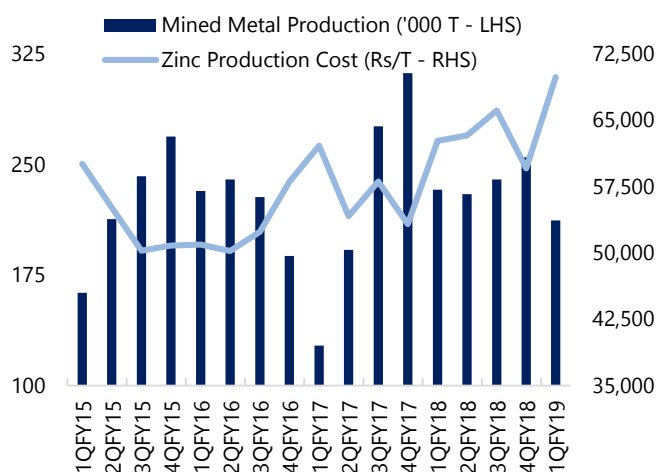
Source: Company, Kotak Securities – Private Client Research

Lower volume and higher cost of production impacted performance

HZ reported EBITDA of Rs27.13bn, up 13.8% YoY (down 25.1% QoQ), with an EBITDA margin of 51.1%, down 660 bps QoQ. The sequential decline in operating performance was on account of lower volume and increased in cost of production, which offset the benefit of higher zinc LME price and rupee depreciation. The company's mined metal production declined 9% YoY to 212,000 tons (down 17% QoQ) due to closure of open cast operations. The led to 11%/17% YoY/QoQ decline in refined zinc output to 172,000 tonnes, lead output decline to 42,000 tonnes due to maintenance related shutdown, as a result silver output declined to 138 tonnes.

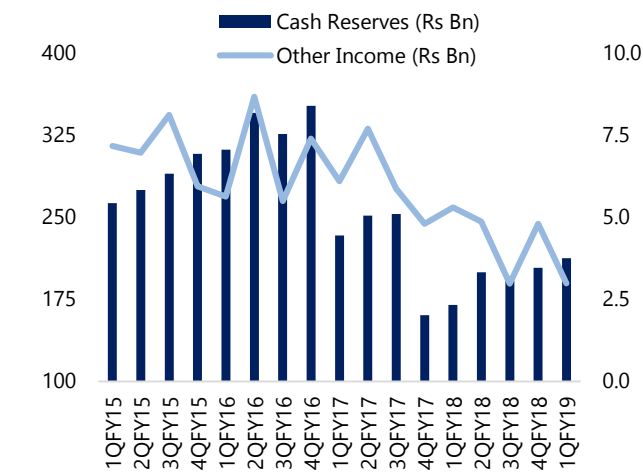
The cost of production during the quarter increased 17% QoQ to Rs69,907/tonne (US\$1,043) due to lower volumes, higher power & maintenance costs and impact of wage settlement. The company concluded a five year wage settlement which resulted in costs increasing by US\$33/tonne. Management maintains their FY19 guidance of US\$950-970/tonne as cost of production.

Mined Metal production as per plan



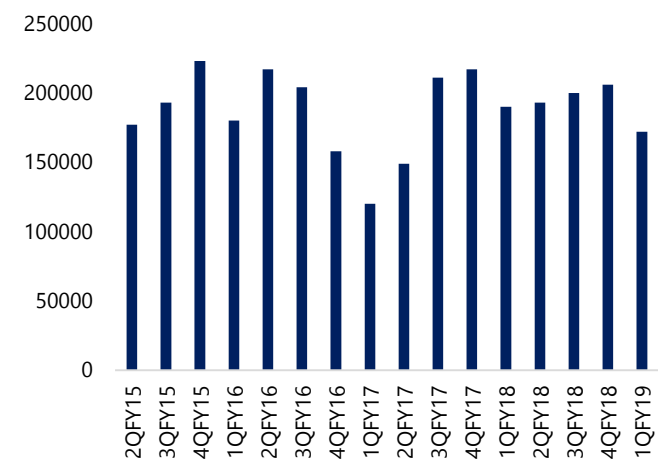
Source: Company

Cash and cash equivalents at Rs213bn



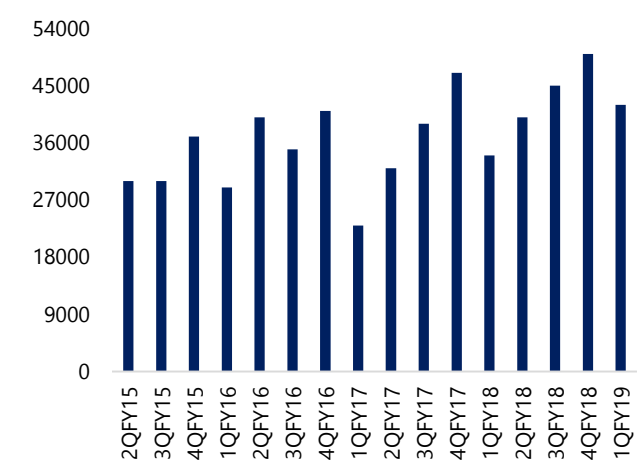
Source: Company

Zinc Volume trend (tonnes)



Source: Company

Lead sales volume (tonnes)



Source: Company

Lower demand led to surplus in 1QCY18; ILZSG forecast deficit for 2018

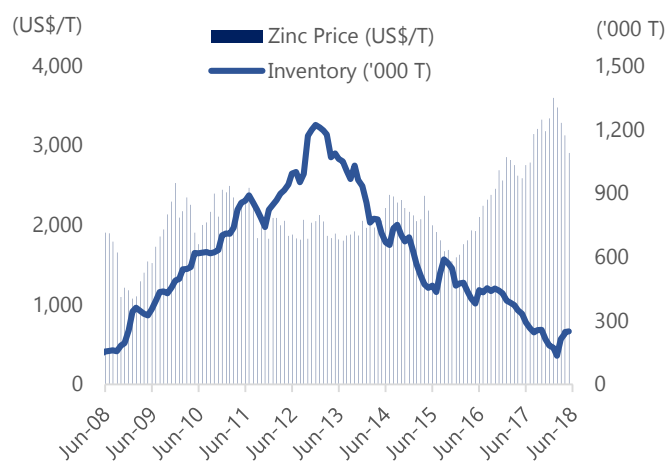
Zinc demand-supply

(MT)	Jan - Mar	
	2017	2018
Mine Production	3.08	3.09
Metal Production	3.25	3.31
Metal Usage	3.27	3.28
Surplus / (Deficit)	(0.02)	0.03

Source: ILZSG

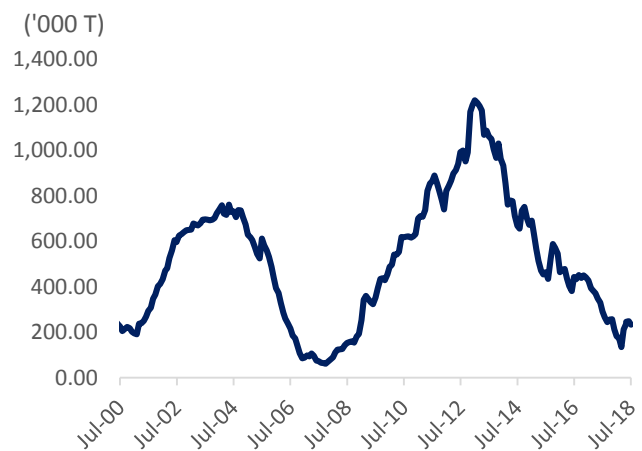
As per International Lead and Zinc Study Group (ILZSG), global demand for refined zinc metal will comfortably exceed supply in 2018, with the extent of deficit at 263,000 tonnes. However, in 1QCY18 the global refined metal was in surplus to the tune of 25KT, with an inventory, increasing by 118KT, during the same period. The surplus was on account of lower demand in Europe, Japan, Taiwan (China) and the United States, compared to 1QCY17. Zinc mine production was largely flat, while metal production was up 1.7% YoY. The recent fall in the zinc prices was backed by surplus in 1QCY18 and rising inventories. Going ahead, with the expectation of markets to remain in deficit and possibility of declining inventory will worsen the supply situation and keep LME prices firm in the near term.

Zinc price and inventory trend



Source: Bloomberg, Kotak Securities – Private Client Research

Inventory increased on lower demand



Source: Bloomberg, Kotak Securities – Private Client Research

Other Highlights

- HZ had residual hedges of 70kt for Zn at US\$3,076/t and 15kt for lead at US\$2,374/t. The hedging loss accounted in 1QFY19 is US\$42 mn. There are no forward sales position as of now.
- Availability of linkage coal during the quarter was ~7% as against the expectation of 40-42%, due to evacuation issues at the subsidiary of Coal India.
- The company received Environment Clearance (EC) at the Sindesar Khurd (SK) mine from 4.5MT to 6MT capacity.
- The Chanderiya zinc-lead pyrometallurgical smelter is being modified to produce standalone lead to cater to the increasing lead mined metal output.
- The cash reserves increased to Rs213 bn in June 2018 (Rs50/share) from Rs204 bn at the end of Q4FY18. We note that company earned a cash profit of Rs23 bn during the quarter.
- Management expects zinc fundamental to continue to remain strong in the medium term due to tight supply and increasing demand from galvanizing sector. The Industry expects zinc refined metal demand to grow at 2% annually for the next 5 years.

Recommend BUY

We like HZL for its strong fundamentals with structurally positive pricing scenario for zinc and lead globally due to mining supply cuts. The stock has corrected since our last recommendation (Reduce at CMP Rs.308) and now is trading at 6.2x/5.6x FY19E/FY20E EV/EBITDA, which in our view is attractive. Hence, we upgrade the stock to BUY, with a revised target price of Rs300 (earlier Rs318).

Company Background

Hindustan Zinc is a Vedanta Group company in zinc, lead and silver business. The company is one of the world's largest integrated producers of zinc and are among leading global lead and silver producers. HZ is also one of the lowest cost producers in the world and are well placed to serve the growing demand of Asian countries. Core business comprises of mining and smelting of zinc and lead along with captive power generation. The company has a metal production capacity with a key lead-zinc mines in Rampura Agucha and Sindesar Khurd; and key modern smelting complexes in Chanderiya and Dariba, all in the state of Rajasthan in India.

Financials: Consolidated

Profit and Loss Statement (Rs mn)

(Year-end March)	FY17	FY18	FY19E	FY20E
Net sales	187,980	225,210	259,484	272,056
Growth (%)	32.1	19.8	15.2	4.8
Operating expenses	90,596	102,490	119,237	123,893
EBITDA	97,384	122,720	140,247	148,163
Growth (%)	46.6	26.0	14.3	5.6
Depreciation & amortisation	18,112.2	14,830.0	18,070.4	20,070.4
EBIT	79,272	107,890	122,177	128,093
Other income	24,737.2	17,510.0	11,861.0	13,611.0
Interest paid	2,017	2,830	2,547	2,292
Exceptional Items	0.0	2,400.0	0.0	0.0
PBT	101,992	124,970	131,491	139,411
Tax	18,836.5	32,210.0	35,502.6	37,641.0
Effective tax rate (%)	18.5	25.8	27.0	27.0
Net profit	83,156	92,760	95,988	101,770
Minority interest	0	0	0	0
Adjusted Net profit	83,156	92,760	95,988	101,770
Growth (%)	1.8	11.5	3.5	6.0

Source: Company, Kotak Securities – Private Client Research

Cash flow Statement

(Year-end March)	FY17	FY18	FY19E	FY20E
Pre-tax profit	101,992	124,970	131,491	139,411
Depreciation	18,112	14,830	18,070	20,070
Chg in working capital	34,909	(57,476)	336	(2,959)
Total tax paid	18,837	32,210	35,503	37,641
Other operating activities	(25,077)	4,400	2,547	2,292
Operating CF	111,100	54,514	116,942	121,174
Capital expenditure	(23,216)	(31,903)	(24,800)	(25,000)
Chg in investments	113,997	35,607	(35,000)	(35,000)
Other investing activities	-	-	-	-
Investing CF	90,782	3,703	(59,800)	(60,000)
Equity raised/(repaid)	-	-	-	-
Debt raised/(repaid)	80,005	(80,005)	-	-
Dividend (incl. tax)	(145,342)	(39,549)	(49,436)	(49,436)
Other financing activities	(2,017)	(2,830)	(2,547)	(2,292)
Financing CF	(67,354)	(122,383)	(51,983)	(51,728)
Net chg in cash & bank bal.	134,528	(64,166)	5,159	9,446
Closing cash & bank bal	83,803	19,637	24,796	34,242

Source: Company, Kotak Securities – Private Client Research

Balance sheet (Rs mn)

(Year-end March)	FY17	FY18	FY19E	FY20E
Cash & Bank balances	83,804	19,640	24,796	34,242
Other Current assets	38,201	40,160	50,753	56,786
Investments	237,827	202,220	237,220	272,220
Net fixed assets	128,145	145,219	151,948	156,878
Goodwill & intangible assets	0	0	0	0
Deferred Tax Asset	21,915	22,080	24,288	24,288
Total assets	509,891	429,319	489,005	544,414
Current liabilities	124,338	69,997	83,126	86,200
Borrowings	80,005	0	0	0
Other non-current liabilities	0	0	0	0
Total liabilities	204,342	69,997	83,126	86,200
Share capital	8,451	8,451	8,451	8,451
Reserves & surplus	297,099	350,870	397,422	449,757
Shareholders' funds	305,549	359,321	405,880	458,214
Minority interest	0	0	0	0
Total equity & liabilities	509,892	429,318	489,005	544,414

Source: Company, Kotak Securities – Private Client Research;

Ratio Analysis

(Year-end March)	FY17	FY18	FY19E	FY20E
Per Share (Rs)				
EPS	19.7	22.0	22.7	24.1
DPS	29.4	8.0	10.0	10.0
Book value	72.3	85.0	96.1	108.4
Valuation (x)				
P/E	13.6	12.2	11.8	11.1
Price/Book value	3.7	3.2	2.8	2.5
EV/EBITDA	9.1	7.4	6.2	5.6
EV/Sales	4.9	4.0	3.4	3.1
Profit ratios (%)				
RoE	28.0	26.4	24.2	22.6
RoCE	22.0	26.4	24.1	22.6
Margin (%)				
EBITDA	51.8	54.5	54.0	54.5
EBIT	42.2	47.9	47.1	47.1
PAT	44.2	41.2	37.0	37.4
Turnover Days				
Inventory	38.8	22.2	25.0	25.0
Debtors	2.7	3.0	5.0	5.0
Creditors	495.8	241.5	241.0	241.0

Source: Company, Kotak Securities – Private Client Research

Forthcoming events

Date	Event
24-Jul	Asian Paint, Century Ply, Kajaria Ceramics, Radico Khaitan earnings expected
25-Jul	Crompton Greaves, Hero MotoCorp, JSW Steel, KPIT, L&T earnings expected
26-Jul	Biocon, Colgate Palmolive, Concor, Dr. Reddy's, Eveready Ind, ITC, Jindal Stainless (Hisar), Maruti Suzuki India, Petronet LNG, Tata Power earnings expected
27-Jul	Bank of Baroda, Genus Power, HCL Tech, ICICI Bank earnings expected
28-Jul	Balmer Lawrie, JK Cement, Persistent earnings expected
30-Jul	Axis Bank, GSPL, HDFC, IDFC, IDFC Bank, Shree Cement, Tech Mahindra earnings expected
31-Jul	BEL, Bludart, Castrol India, Dabur, MGL, Redington, Supreme Ind, Tata Motors, Tech Mahindra, Vedanta,

Source: www.bseindia.com

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Definitions of ratings

BUY	– We expect the stock to deliver more than 12% returns over the next 12 months
ACCUMULATE	– We expect the stock to deliver 5% - 12% returns over the next 12 months
REDUCE	– We expect the stock to deliver 0% - 5% returns over the next 12 months
SELL	– We expect the stock to deliver negative returns over the next 12 months
NR	– Not Rated. Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.
SUBSCRIBE	– We advise investor to subscribe to the IPO.
RS	– Rating Suspended. Kotak Securities has suspended the investment rating and price target for this stock, either because there is not a Sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.
NA	– Not Available or Not Applicable. The information is not available for display or is not applicable
NM	– Not Meaningful. The information is not meaningful and is therefore excluded.
NOTE	– Our target prices are with a 12-month perspective. Returns stated in the rating scale are our internal benchmark.

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